

12A 64707

PROJECT ASSISTANCE COMPLETION REPORT

TO: The Files

FROM: Bernai Velarde, PSP *AMM*

SUBJECT: Close Out Report for the Small Business Development Project No. 522-0205

DATE: May 8, 1990

A. BACKGROUND

In 1984 the Agency for International Development signed the Small Business Development Project (SBD) (No. 522-0205) with the Government of Honduras under which a total of \$721,000 in AID funds eventually was obligated. The Project was designed to improve small business development in Honduras, generate employment and further the country's economic development given the problems and importance of the enterprises in the economy, growing unemployment, the stagnation of large scale industry and the expanding private sector interest in helping small and medium scale enterprises.

In order to increase production and employment in the businesses, the project provided assistance for the development of a source of financial and technical assistance for small and medium scale entrepreneurs in Honduras that had no access to the banking system. For this purpose, two Honduran private organizations were chosen to implement the project: The Financiera Industrial y Agropecuaria (FIA) as the finance company and the National Association of Industrialists (ANDI) as the Technical Assistance System Coordinator.

B. PROJECT GOAL AND PURPOSE:

The goal of the project was to increase production and employment in small and medium scale enterprises.

The purpose of the project was to develop a source of accessible financial and technical assistance for Honduras' small and medium scale entrepreneurs. By the end of the project, a well managed small business finance company was to

have been established and have developed a loan portfolio of L12.7 million. In addition, a program to provide competent and appropriate technical assistance to small enterprises was to have been developed.

C. PROJECT DESCRIPTION:

The Project activities were the following:

1. Credit Assistance for Small Enterprises

Five Honduran banks agreed to organize and capitalize a commercial finance company called Financiera Industrial y Agropecuaria, S.A. (FIA) with an authorized capital of L2.0 million. The five banks were Banco de Occidente,

Banco de los Trabajadores, Banco Hondureño del Café, Banco Financiera Centroamericana and Banco Mercantil. FIA's purpose was to provide credit, services, and financial advice to small and medium scale enterprises. To assist FIA in establishing its credit program, the Government of Honduras agreed to provide the local currency equivalent to \$4.0 million through the National Industrialist Fund (FONDEI) from a Special Account established under the A.I.D. supported Economic Recovery Program. The funds were provided to FONDEI without interest and FONDEI in turn gave FIA a twenty year loan with an eight year grace period at the highest Central Bank discount rate which was 9 percent. The interest earned by FONDEI on its loan to FIA were used to cover the cost of the Business Assistance System.

Under its credit program, FIA provided financing to private entrepreneurs in the industrial, agricultural, commercial and service sectors. FIA's borrowers were sole proprietors, partnerships, corporations, and cooperatives engaged in, or who wished to start industries and service sector operations. Loan funds would be used for expansion of and new investment in productive capacity and working capital purposes. Uses of funds would include operating costs; raw materials; professional services; leasehold improvements; machinery; equipment and spare parts; and, under carefully controlled conditions, vehicles and buildings.

2. Technical Assistance For Small Entrepreneurs

Small and medium scale enterprises were found to be deficient in management and technical skills. Specifically, these weaknesses were found to be in record keeping, planning, marketing and market analysis, management and production controls and legal organization. Thus, technical assistance would be provided through training and/or management assistance in management tools, training and/or management assistance in business planning, technical information, legal assistance and valuation of assets.

a. The Business Assistance System (BAS)

The Business Assistance System (BAS) that would be developed through the project would start by supporting institutions that had shown their interest and capability in providing services needed by small businesses. The BAS would establish a permanent network of organizations providing technical assistance to the small and medium-size entrepreneurs. The BAS would generate numerous clients for FIA and provide individual technical assistance to them as well.

b. The Technical Assistance System Coordinator

The Coordinator would assess the management, information, and technical assistance needs of small and medium enterprises, finance the assistance activities of the institutions it would qualify as service providers, evaluate the effectiveness of those institutions and increase resources for the most effective operations, qualify new organizations to participate in the system, train the personnel of and ensure coordination among all service providing agencies.

An AID Grant in the amount of \$600,000 provided in June 1984 with an original PACD date of May 31, 1987. Subsequently, AID increased the amount by \$200,000 for a life of project funding of \$800,000, and extended the PACD to May 30, 1988. The PACD was again extended to May 30, 1989 so as to continue to fund ongoing project activities and insure a smooth phase in with the Small Business II Project (SBII).

The Grantee Counterpart Contribution was the equivalent of \$5,400,000 in local currency which provided loan funds to FIA (\$4,000,000 equivalent) and program expenses for ANDI (\$1,400,000 equivalent).

D. MAJOR OUTPUTS:

The outputs listed below are drawn from FIA and ANDI's final reports and are compared to planned LOP targets.

<u>OUTPUTS</u>	<u>INDICATORS</u>	<u>PLANNED LOP</u>	<u>ACCOMPLISHMENTS CUMMULATIVE</u>
To increase production & employment in small- & medium-sized enterprises	Finance company established	1	1
	Amount of FIA's loan portfolio	L12.7M	9.2
	Number of Loans	170	332
	Value-added to national production	12.6M	12.0
	FIA's jobs maintained	-	1,000
	FIA's increase in employment	500	950
	ANDI/PYME's* jobs	N/A	5,266
	BAS participating organizations	6	22
	Small- and medium-sized enterprises receiving technical assistance	525	3,746

* PYME: Pequeña y Mediana Empresa

E. INPUTS:

AID would provide \$600,000 in Grant Funds. By the PACD, this amount was increased to \$800,000. The Grantee Counterpart Contribution was the equivalent of \$5,400,000 in local currency.

F. OUTPUTS PLANNED BUT NOT ACCOMPLISHED:

Only one important planned output was not accomplished under the project. FIA reached a loan portfolio level of L9.2 Million instead of the planned L12.7 Million. USAID/H assumed that FIA would receive L4,000,000 from its shareholders, in the form of loans for cofinancing, to increase its portfolio. However, this cofinancing mechanism did not prove to be feasible under the project.

G. FINANCIAL STATUS:

The total dollar amount authorized and obligated was \$800,000. The total dollar amount disbursed was \$720,916 and the total dollar amount to be deobligated is \$79,084. The total ESF Lempira amount authorized and obligated was L11,127,000; L2,000,000 were from Project No. 522-ESF-0283 and L9,127,000 were from Project No. 522-ESF-0230. The total ESF Lempira amount disbursed was L11,100,200.

H. ADJUSTMENTS IN PROJECT DESIGN:

In 1986, FIA proposed that it be allowed to establish an interest rate policy which would be more competitive in the market and responsive to its target group, without having to maintain a minimum eight point spread as stipulated in the original project agreement. On September 9, 1986 AID authorized FIA to set their own interest rates consistent with current market rates.

As a result of an interim evaluation of the project, by Nathan Associates, Inc., on August 21, 1987, AID amended the Small Business Development Agreement to eliminate the financial linkage between FIA and ANDI. ANDI would no longer receive the spread generated by the loan that FONDEI made to FIA. FIA would now be authorized to use this spread for technical assistance and the execution of other subprojects developed by FIA and agreed to by AID. This enabled FIA to start up its own technical assistance unit. ANDI would continue to develop the BAS for other micro and small-scale business organizations and would rely on GOH grant funding.

I. RESULTS OF EVALUATIONS:

Overall, the Nathan evaluation on the Small Business Project (No. 522-0205) indicated that FIA was a sound financial institution which operated in a financially responsible and conservative manner. The evaluation also indicated that the PYME unit in ANDI had a good administrative system control and had shown a lot of progress towards the small business sector at both the program and institutional level. Both FIA and PYME's staff were considered highly qualified.

Bellow are the most important recommendations of the Nathan Evaluation that were approved by the Mission:

1. Complete the separation of FIA and ANDI/PYME activities.
2. Undertake a market analysis to determine market segment and niche for FIA.
3. Charge interest rates to reflect FIA's cost of money and on-lend at competitive rates.
4. Investigate the feasibility of opening a window for small business and micro production enterprises in FIA.
5. Develop the planned cofinancing with FIA shareholders.
6. Vest final authority for approval of loans of L 100,000 or less in FIA management.
7. Develop loan performance incentives and disincentives to decrease loan arrearages; establish policy and procedures for writing off bad debts.
8. Standardize FIA financial statement requirements to include data sufficient to calculate the financial and economic rates of return.
9. Develop a long-term strategic plan for PYME to set program priorities, determine technical assistance needs and diversify sources of funding.
10. Redefine PYME job descriptions to match actual duties and team approaches used; develop staff training plan.
11. Strengthen the PYME interorganizational network by (a) offering management assistance to PVO's and (b) joint course offerings for beneficiaries.
12. Encourage a more active role on the part of PVO's in client and staff development needs, assessment, course design and implementation in the PYME program.

All the above recommendations have been closed except for item No. 5 which refers to cofinancing with FIA shareholders and which was not considered feasible under the project.

J. SUMMARY OF LESSONS LEARNED:

- 1) In order to prevent slow project start-up and other problems, AID should ensure that the executing agencies have established development programs and have strong management track records, that they are strong institutionally and that they participate in project design. FIA was a newly constituted finance company and ANDI had no established development programs prior to this Project. Under these circumstances, the need to define internal procedures and negotiate agreements with several organizations was time consuming. No feasibility study reviewed ANDI's institutional capacity to manage the PYME project and ANDI did not participate in the early design phase of the project.

- 2) Many times, the PYME Committee members have appeared to be more interested and committed to small business development than the majority of the ANDI members. This is probably because PYME was created by ANDI in response to an AID initiative. Ideally, AID should support programs that grow out of the commitment of a group.
- 3) Since the PADF Advisor's contract was with AID and he was not paid by ANDI/PYME, he was not accountable and responsible to ANDI. This led to some confusion regarding the advisor's role and responsibilities. In the future, AID should allow more involvement of the NGO in writing the job descriptions and finalizing a local contract between the advisor and the host organization. AID should also provide for some in-country costs to be paid directly by the host organization.